ERISA Advisory Council
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Written Statement On

Mandated Disclosure for Retirement Plans – Enhancing Effectiveness for Participants and Sponsors

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On behalf of the Society of Actuaries and myself, I would like to thank you for the opportunity to present observations from research sponsored by the Society of Actuaries. The following is a summary of the research conducted with pre-retirees and retirees on their perception and management of risks in retirement. The information is presented to inform the ERISA Advisory Council on their review of "Mandated Disclosure for Retirement Plans – Enhancing Effectiveness for Participants and Sponsors".

Society of Actuaries Post-Retirement Needs and Risks Research

The Society of Actuaries Committee on Post-Retirement Needs and Risks (CPRNR) has been working for nearly 20 years to identify and understand the way Americans manage their finances post-retirement. This work includes eight biennial surveys of the public's knowledge and perceptions about post-retirement needs and risk management. A major finding from this work is that planning often tends to be short term and cash flow focused, and that many people do not focus on risk or plan for shocks.

In 2015, the Society of Actuaries sponsored retirement risk research consisted of three components – a Survey of Post-Retirement Risk and the Process of Retirement (surveying U.S. pre-retirees and retirees), focus groups looking at experiences of U.S. and Canadian individuals who had been retired 15 years or more and were resource constrained in the amount of assets and regular income they had in retirement, and in-depth interviews with caregivers of people who need substantial care and would not have generally fit into the focus group population.

In 2013, the Society of Actuaries sponsored a series of focus groups with people who had retired in the prior 10 years and who self-described they chose to retire (i.e. not forced to retire due to health, disability or job loss) and were resource constrained in the amount of assets and regular income they had in retirement. The study discovered a lack of planning and a general tendency to adjust to events as they occur.

The research of the CPRNR can be obtained from the Society of Actuaries website at https://www.soa.org/research/topics/research-post-retirement-needs-and-risks/. The research findings presented below are taken from reports found in the tab for Retirement Risk Survey Series.

Findings from the Research

When people are planning for retirement, many risks in retirement must be considered. Three key items that are basic to retirement planning are to plan for a long time horizon (i.e. to end of life), to consider daily expenses along with other non-daily expenses that will most likely occur, and to have sufficient assets and income to cover these items. Based on the survey and personal responses in interviews and focus groups, the research documented the following items of concern:

Planning for retirement is short term and cash flow focused:

Three top concerns consistently appear, namely, inflation, health care expenses and long-term care expenses – although planning for these is not necessarily considered

Retirees retired at a median age 60 but pre-retirees expect to retire at a median age 65 – creating a gap in knowledge between the groups

Planning horizons of a median 10 years are short for a retiree's potential longevity

Risk management strategies for retirees are to reduce their spending, increase their savings and pay off debt

Financial shocks and unexpected expenses are not fully considered in their planning:

Home repairs and major dental expenses are unexpected expenses most mentioned – both of which could be expected

The rising costs of housing, especially taxes and upkeep, are also mentioned

Multiple shocks accumulate to a bigger problem than a single shock – the effect of shocks may take time before they create a crisis in living standards

Due to financial shocks the research indicates:

Assets were significantly reduced for 1/3rd of the retirees

Spending was significantly reduced for 1/10th of the retirees

Very few have emergency funds set aside for unexpected expenses

About 1/5th could not spend more than $1,000 without harming their security

Retirees are resilient:

At least 3/4th of retirees were able to manage somewhat in their new financial constraints

Long term care and divorce were shocks that caused the most significant issue

Children needing longer term support was also a major issue

How Retirees Make Decisions

As mentioned above, retirees are resilient and attempt to manage within their financial constraints. Some of the ways they manage are:

They carefully manage regular expenses – many considered themselves to be thrifty and frugal and manage to their "needs" more than their "wants"

They attempt to live from regular income (annuities, Social Security and investment income) and spend their Required Minimum Distributions

They do not want to spend down their assets – spending their Required Minimum Distributions was not considered spending down their assets

They adjust to events as they occur and reduce spending if needed to preserve assets

Deficiencies Retirees Are Facing

Retirees may hold some misperceptions about retirement security. A decline in their cognitive abilities as they age may serve to complicate these misperceptions and the issue of retirement security more. The Society of Actuaries sponsored research on this topic indicates there are gaps in knowledge and is summarized below:

Retirees may save too little before retiring and create the need to rely more on Social Security.

Retirees may underestimate how much money is needed for retirement. Often retirees conduct very little or ineffective analysis of their finances before deciding to retire.

Retirees may underestimate their longevity and plan for a shorter time horizon than their expected lifetime. Thus, they risk living longer than they planned and a potential crisis in their living standard later in life.

Most retirees are self-insuring for a long life. They do not purchase annuities to protect their income or insure or consider the costs of living assistance and long-term care.

Many retirees do not fully plan for income and expenses throughout their retirement in one or more of the following ways:

> Only basic living costs are fully considered and inflation may not be included in their planning
>
> Emergency funds are lacking and unexpected expenses may not be included in their planning
>
> Reliance on Social Security plus Minimum Required Distributions becomes their default income plan
>
> While they desire to preserve their assets, they do not have a real plan in place to do so
>
> Some are spending retirement assets on children and grandchildren without considering their own long term needs

Many do not have the financial literacy to handle managing finances over the long term:

> Many lack an understanding of investing for income over long periods of time and many retirees lack basic math skills to understand investing concepts
>
> Many lack understanding of asset allocation and investment risks
>
> Many lack a basic understanding of annuity products and the annuity marketplace

Effect on Employee Communications and Disclosures

The views and opinions expressed in this section are based on my own perspective only and are not statements of nor endorsed by the Society of Actuaries as a whole.

Based on my experience, following are some ideas that I personally have to aid employers and regulators in designing employee communication programs and plan disclosures.

The material needs to be part of a broader approach to financial wellness. In designing and positioning the material, employers could:

Position the SPD and other employee communication as part of financial wellness education

Improve the financial analysis of people before they choose to retire to allow for them to better plan and prepare for retirement

Consider the level of knowledge and misperceptions of the intended audience - documents written in a manner that alludes their level of knowledge are ineffective and similar to reading in a foreign language

Plan material should emphasize the benefits claiming decisions with the intentions of making people think more about how and when they are choosing their benefits:

Consider education on Social Security and benefit claiming options

Educate on need for reliable income in retirement and annuities as an option

Communications should encourage long term planning:

Emphasize the need to start saving early and increasing saving over time

Integrate other monies held by participants into the planning process

Discuss longevity and planning for a longer horizon

Communication should encourage people to set aside emergency funds beyond saving for retirement:

Educate on the effects on retirement income of borrowing from their retirement assets

Educate on the effects on retirement income of withdrawing and spending their retirement assets

I encourage you to review this research and am available to discuss this information and to assist you in locating other information from the CPRNR research.

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